No. 21037

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

UNIVERSITY PROPERTIES, INC.,

Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

ON PETITION FOR REVIEW OF THE DECISION OF THE TAX COURT
OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

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OPINION BELOW

The opinion of the Tax Court (R. 24-37) is reported at 45 T.C. 6.

JURISDICTION

By a statutory notice (R. 7-11) issued under date of April 20, 64, pursuant to Section 6212 of the Internal Revenue Code of 1954, e Commissioner of Internal determined deficiencies in federal income xes against University Properties, Inc. (herein sometimes referred as the taxpayer), for the fiscal years ended October 31, 1961 and 62, in the respective amounts of $40,114.29 and $38,573.53. A timely tition for redetermination of such deficiencies (R. 2-6) was filed the taxpayer with the Tax Court on July 16, 1964, pursuant to ction 6213 of the 1954 Code. The issues involved were submitted to e Tax Court on a stipulation of facts (R. 19-22) and documentary hibits (not included in the duplicated record). On January 31, 1966,

the Tax Court filed its opinion (R. 24-37) affirming the Commissioner's determination, and on February 1, 1966, entered its decision (R. 38) redetermining deficiencies for the taxable years in issue in the respective amounts determined by the Commissioner. The taxpayer's petit for review of the Tax Court's decision by this Court (R. 39-42) was timely filed on April 27, 1966. Jurisdiction is conferred on this Court by Section 7482 of the Internal Revenue Code of 1954.

QUESTION PRESENTED

Whether the Tax Court erred in affirming the Commissioner's determination that additional payments of $80,000 made by the taxpayer to its lessor in each of the taxable years in issue, pursuant to a supplemental lease agreement which added additional rental properties to those covered by an existing lease agreement between the parties, are to be amortized over the remaining term of the lease agreement for federal income tax purposes, rather than deducted from gross income in the years of payment, as contended by the taxpayer, as current rental payments or other ordinary and necessary business expenses of the years in which paid.

STATUTE INVOLVED

Internal Revenue Code of 1954:

> SEC. 162. TRADE OR BUSINESS EXPENSES.
>
> (a) In General.--There shall be allowed as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including--
>
> * * *
>
> (3) rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity.
>
> * * *

STATEMENT

This proceeding involves deficiencies in federal income taxes for the fiscal years ended October 31, 1961 and 1962. The facts, supplemented by certain documentary evidence, were stipulated before the Tax Court (R. 19-22), and are summarized in the Tax Court's opinion (R. 24-31).

The taxpayer, University Properties, Inc., was incorporated under the laws of the State of Delaware on July 6, 1953, with authorized capital of 50,000 shares of common stock, par value $1 per share, all issued and outstanding during the period here involved. Since incorporation, its principal office has been at 210 White-Henry-Stuart Building, Seattle, Washington. It filed its federal corporation income tax returns (Exs. 1-A, 2-B) for the years in issue with the District Director of Internal Revenue, Tacoma, Washington. (R. 19, 25.)

The University of Washington originally occupied a 10-acre site which is now in the heart of downtown Seattle. In the 1890's a 583-acre section was purchased and it became the new permanent campus of the University of Washington. In 1902 a small parcel of the original campus was sold to the Federal Government as a post office site. On November 4, 1904, the balance of the tract, commonly known and hereinafter referred to as the Metropolitan Tract, was leased to James A. Moore for a term of 50 years from November 1, 1904. Three years later the lease was assigned to the Metropolitan Building Company, an organization which undertook to erect buildings and otherwise improve the property. That company constructed the White-Henry-Stuart, Skinner, Stimson, Cobb, and Douglas Buildings, and the Olympic Hotel,

including the Metropolitan Theatre, the Olympic Garage and the Cobb Building Annex. (R. 20, 25-26.)

In 1953, the Olympic Hotel and the Metropolitan Theatre, then occupying the entire block on which the Olympic Hotel is situated, were detached from the lease and separately leased to Olympic, Inc. (R. 21, 26.)

On July 18, 1953, a lease (Ex. 3-C) was executed demising the balance of the Metropolitan Tract, including the White-Henry-Stuart, Skinner, Stimson, Cobb, Cobb Annex, and Douglas Buildings, to taxpayer for a term of 35 years from November 1, 1954. (R. 21, 26.) The terms and conditions of this lease agreement are summarized in the opinion of the Tax Court as follows (R. 26-29):

> The term of the lease commenced November 1, 1954, and ends at midnight on October 31, 1989, subject to earlier termination as therein provided. The lease agreed to pay to the lessor as rent for the demised premises a fixed rent in the amount of $1,600,000 for the lease year commencing November 1, 1954, in the amounts of $1,700,000 for the lease years commencing November 1, 1955 and 1956, and in the amount of $1,800,000 for the lease year commencing November 1, 1957. The lessee further agreed to pay a percentage rental for each lease year commencing November 1, 1958, and continuing to the end of the term of the lease, with a minimum guaranteed rental of $1 million per lease year, determined as a percentage of the gross rental income received by the lessee from subtenants for commercial space and a lesser percentage of the gross rental income received by the lessee from subtenants for office space. The percentage rental is not payable on miscellaneous income of the lessee derived from other sources of business activities, such as resale of public utilities, linen and supple services, janitor services, etc. The lease stated that it was understood that all the rentals provided therein were predicated on the assumption that the entire demised premises would be capable of being occupied, operated, or used by the lessee at all times; and if for any reason other than default of the lessee any portion of the demised premises should not be capable of being occupied, operated, or used by the

lessee, the annual minimum guaranteed rental should be reduced for the period of time said space remained untenantable in the amount which would have been the lessor's percentage rental from the untenantable space if said space had been tenantable, and the fixed annual rental should be reduced in a like amount if the situation developed in the first 4 years. The lessee agreed to manage and operate the various buildings on the demised premises as a center of store and office buildings of the first class in the city of Seattle. The lessee also agreed to modernize the buildings on the demised premises and to expend in such modernization at lease $2 million, such modernization program to be commenced promptly upon entering into possession of the demised premises and to be completed if reasonably possible on or before November 1, 1958. The lessor agreed to create a "New Building Fund" and to pay a percentage of the gross rental income it received from the demised premises, limited to a certain amount per year, into the fund, which was to be used to reimburse the lesee for the modernization expenditures heretofore mentioned and for the construction of new buildings and major improvements and additions to the property. The lessee agreed to study from time to time the desirability and economic necessity for the construction of new buildings and capital alterations, and to make recommendations to the lessor with reference thereto. The lessor had the right to determine what buildings and capital improvements would be made, and the lessee was to be responsible for the construction of such buildings and improvements with the right to be reimbursed from the New Building Fund for the cost thereof. The lessee also agreed to expend not less than 4 percent of its gross rental income from the demised premises for maintenance and repair of the buildings and improvements on the demised premises. The lessor was given the right to cancel the lease upon 12 months' notice if at any time during the term of the lease the lessor should become liable for the payment of Federal income tax on all or any part of its income thereunder and the parties should be unable to arrive at a mutually satisfactory modification of the lease terms compensating for such tax liability, in which event the lessor shall pay to the lessee specified sums for each quarterly rental payment that shall have been made under the lease. Upon termination of the lease the lessee shall surrender the demised premises, together with any of the lessee's improvements, fixtures, and any new buildings and capital alterations which may be constructed upon the demised premises during the term of the lease, in as good condition and repaid as when received. Provision was also made for termination of the lease by the lessor in the event of default on the part of the lessee.

On January 29, 1958, the University of Washington reacquired from the United States Government a part of the post office site which had been carved out of the original Metropolitan Tract in 1902. As consideration for this land, the University of Washington agreed with the United States Government through the General Services Administration to demolish the old post office building and to construct a new post office on that part of the site retained by the Federal Government. Certain easements were also exchanged in the transaction. (R. 21, 29.)

On February 5, 1958, a supplemental lease agreement (Ex. 4-D) from the University of Washington to the taxpayer added this newly acquired property to the properties covered by the 1953 lease. (Stip. par. 9, following R. 21; R. 29.) 1/ After reciting execution of the lease agreement of July 18, 1953; its requirement that the taxpayer operate the various structures and buildings then or thereafter constructed upon the demised premises in such a manner as not to injure the reputation thereof and to maintain the demised premises as a center of store and office buildings of the first class and at the same time to so operate the tract as to produce the maximum return consistent with the character of the tract; and that the parties had determined that, in order to accomplish these purposes and to produce a maximum return for the lessor and to preserve and improve the status of the tract as a business enter of the first class, the contemplated new building to replace the existing Douglas Building should be located on its present site enlarged by the addition of the part of the post office tract, described therein, the supplemental lease agreement continued as follows (Ex. 4-D, pp. 2-3):

1/ Page 4 of the stipulation of facts, following R. 21, was omitted in the Tax Court Clerk's pagination of the record as certified to this Co

AND WHEREAS, Article VII, Section 3 of said lease provides that all new buildings upon completion shall be subject in all respect to the rights and obligations of the parties as set forth therein with respect to the original structures upon the demised premises; and

WHEREAS, the Lessor has now acquired the above described tract (being a portion of the present post office site) under and pursuant to a contract designated as GS-RIO-SWPO-A entered into by the Lessor with the General Services Administration of the United States of America as of October 18, 1957, under which said contract Lessor has undertaken and agreed to demolish the present post office building and to construct a new post office building for the United States of America; and

WHEREAS, Lessor entered into said contract with the General Services Administration of the United States of America upon the understanding and agreement with Lessee that the portion of the present post office site and the rights and privileges in connection therewith to be acquired by the Lessor would be added to and incorporated in the Metropolitan Tract area covered by said lease of July 18, 1953, subject to all of the terms and conditions of said lease, and that in consideration therefor Lesee would undertake to fulfill and perform all of Lessor's undertakings and agreements with respect to the construction of the new post office building for the United States of America.

NOW, THEREFORE, in order to confirm the inclusion of the above described tract within the demised premises and to confirm said understanding and agreement, it is agreed that:

1. The tract of land described above shall be deemed to be a part of the demised premises covered by said lease of July 18, 1953, and any new structure located thereon shall be subject in all respect to the rights and obligations of the parties as set forth in said lease with respect to the original structures upon the demised premises. Without limiting the generality of the foregoing provision relating to the application of the terms of said lease to the tract of land described in this Supplemental Lease and structures thereon, it is specifically agreed that monies in the New Building Fund provided for by Article VII of said lease dated July 18, 1953, may also be expended with respect to the tract of land described in this Supplemental Lease and structures thereon, for the same purposes and in accordance with those same provisions of said lease of July 18, 1953, which govern expenditures out of the New Building Fund with respect to the demised premises, initially described in said lease, and structures thereon.

other consideration, to make three such $80,000 payments "as additional rentals over and above all rentals provided for under the term of" the original lease, which applied to the newly added property in all respects as to the original leasehold. The Commissioner of Internal Revenue disallowed such deductions on the ground that the $80,000 payments "did not represent a current rental payment but a capital expendi or advance rental not deductible in the year paid," and allowed, instead, a deduction in the nature of an amortization deduction based on prorating such payments over the unexpired term of the original lease at the time the payments were made.

The Commissioner's determination is prima facie correct and the burden was upon the taxpayer to prove that the payments were in fact "rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not or is not taking title or in which he has no equity" within the meaning of the statutory provision on which its claim of eduction is primarily based, or that such payments were in fact "ordinary and necessary expenses paid or incurre during the taxable year in carrying on any trade or business" within the meaning of the statutory provision on which its claim of deduction id secondarily based.

The taxpayer has failed to prove that the payments are deductible under either provision of the applicable statute. It has proved payment of the amounts in issue, and admittedly the taxpayer had not taken and was not taking title to and had not equity in any of the property under lease. It has been judicially determined, however, tha

to be deductible as rent the amount claimed must have been paid as rent in fact, rather than a payment of a different character under the guise of rent. Moreover, such payment must be shown to have been made for the use or possession of the property with respect to the year in which the payment is claimed as a deduction. Payments of advance rental, like payments made to obtain a lease, or payments made by a lessor to procure a lease of his property, are not deductible in full, but must be deducted pro rate over the life of the lease in the form of amortization deductions.

The evidence in this case does not support the taxpayer's contention that the $80,000 "additional rentals" payments made under its supplementary lease constituted rental for the respective years of payment. Rather, the evidence is consistent only with the Commissioner's determination, affirmed by the Tax Court, that the payments were capital expenditures or advance rentals paid as consideration for the inclusion of the additional property in the taxpayer's leasehold.

Likewise, the evidence does not support the taxpayer's contention that the payments in issue represented ordinary and necessary business expenses of the years in which they were made.

ARGUMENT

THE TAX COURT DID NOT ERR IN HOLDING, UNDER THE STIPULATED FACTS, THAT THE ADDITIONAL PAYMENTS OF $80,000 MADE BY THE TAXPAYER IN EACH OF THE TAXABLE YEARS WERE NOT DEDUCTIBLE IN FULL FROM GROSS INCOME IN THE YEAR OF PAYMENT

It is the taxpayer's contention on this appeal that the amount of $80,000 paid by it to the University of Washington on November 1, 1960, and November 1, 1961, respectively, pursuant to the supplemental lease agreement of February 5, 1958, described in the foregoing statement should be allowed in full as a deduction from gross income under Section 162(a) of the Internal Revenue Code of 1954, supra, in the year of payment, either as rent (Br. 10-24), or, alternatively, as ordinary and necessary business expenses (Br. 24-31), in computing its federal income tax liability for the years in issue.

Section 162(a) of the 1954 Code, under which the deductions here in issue are claimed, provides in material part that in computing taxable income there shall be allowed as a deduction from gross income "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business," including, among other specified expenditures, "(3) rental or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity."

The amounts here in issue were claimed as deductions by the taxpayer on its income tax returns for the years in which the payments were made.(R. 31.) In disallowing the claimed deductions, the Commissioner determined that the payments "did not represent a current rental payment but a capital expenditure or advance rental not deductible in the year paid." On this basis he allowed, instead, as

a deduction for each of the years in issue, in the nature of an amortization allowance, an amount equal to 1/28 of the $80,000 payment made in the fiscal year ended October 31, 1961; and for the fiscal year ended October 31, 1962, he allowed a deduction in the nature of an amortization allowance equal to 1/27 of the payment made in that year. (R. 9, 10.) 2/

The Tax Court held that the taxpayer had failed to establish its right to the claimed deduction, either as rent (R. 32-35) or as ordinary and necessary business expenses (R. 35-37), and affirmed the Commissioner's determination. We submit there is no error in the Tax Court's decision.

Pertinent in the determination of the issues presented by this appeal are certain established principles of law. It long has been settled, for instance, that the Commissioner's determination of an income tax deficiency "has the support of a presumption of correctness, and the petitioner has the burden of proving it to be wrong." Welch v. Helvering, 290 U.S. 111, 115. See also, Wickwire v. Reinecke, 275 U.S. 101, 105; Matern v. Commissioner, 61 F. 2d 663, 666 (C.A. 9th);

2/ The lease of July 18, 1953, expires by its terms at midnight on October 31, 1989 (Ex. 3-C, p. 3). At the time the first $80,000 payment under the supplemental lease of February 5, 1958, because due on November 1, 1960, the original lease had an unexpired term of 29 years; and at the time the second payment was due on November 1, 1962, the principal lease had an unexpired term of 28 years. In his deficiency notice (R. 9, 10) the Commissioner, without explanation, allowed amortization on the basis of unexpired terms of 28 years and 27 years, respectively, which resulted in slightly larger amortization allowances for each year. If this was an error on the Commissioner's part it results in an advantage to the taxpayer and affords no basis for reversing the Tax Court's decision on the merits. Compare Southwestern Hotel Co. v. United States, 115 F. 2d 686 (C.A. 5th), certiorari denied, 312 U.S. 703.

Todd v. Commissioner, 153 F. 2d 553, 557 (C.A. 9th); Clark v. Commissioner, 266 F. 2d 698, 706 (C.A. 9th), and authorities cited.

It also is settled law that deductions from gross income for federal income tax purposes are allowed as a matter of legislative grace and the burden is upon a taxpayer claiming a deduction to prove facts which will bring his claim clearly within the statutory provision authorizing such deduction. New Colonial Co. v. Helvering, 292 U.S. 435, 440; Deputy v. du Pont, 308 U.S. 488, 493; Interstate Transit Lines v. Commissioner, 319 U.S. 590, 593. Under the most liberal expression of the Supreme Court, "Their extent depends upon the legislative policy expressed in the fair and natural meaning" of the provision authorizing the deduction." Lykes v. United States, 343 U.S. 118, 120.

The federal income tax system is based on annual accounting periods, and while income generally is accounted for in the year it is received or accrued and deductions are allowed in the year in which they are paid or incurred, according to the method of accounting regularly employed by the taxpayer in keeping his books, these considerations are qualified by the overall requirement that the method adopted must clearly reflect the income. See Sections 441, 446, 451, 461, and corresponding provisions of prior income tax statutes.

The present case is concerned with the time for taking deductions and in United States v. Ludey, 274 U.S. 295, 304, the Supreme Court said that a taxpayer "cannot choose the year in which he will take a reduction." In Burnet v. Thompson Oil & G. Co., 283 U.S. 301, 306, a case involving oil depletion deductions claimed for the taxable year 1918, the Supreme Court reiterated that "in the absence of express provisions to the contrary, it is not to be supposed that the taxpayer

is authorized to deduct from that year's income, depreciation, depletion, business losses, or other similar items attributable to other years." In a case somewhat analogous to the present case so far as the issue of law is concerned, this Court said in Lichtenberger-Ferguson Co. v. Welch, 54 F. 2d 570, 571-572: "Under whatever system the taxpayer makes its return, the items of income and deductible expenses must have relation to the business done within the year for which the income tax is paid." See, also, Wells Fargo B. & U. Trust Co. v. Commissioner, 163 F. 2d 521, 524 (C.A. 9th); Commissioner v. Boylston Market Ass'n, 131 F. 2d 966, 968 (C.A. 1st).

The deduction, as a business expense, of amounts paid as rent was first specifically authorized in the case of corporations by Section 12(a), first, of the Revenue Act of 1916, c. 463, 39 Stat. 756, and in the case of individuals by Section 214(a)(1) of the Revenue Act of 1918, c. 18, 40 Stat. 1057, and continued through subsequent Revenue Acts, in language identical with Section 162(a)(3) of the 1954 Code relied upon here. The deduction is limited by this provision to "rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity." Compare Oesterreich v. Commissioner, 226 F. 2d 798 (C.A. 9th). As this Court pointed out in Utter-McKinly Mortuaries v. Commissioner, 225 F. 2d 870, 874:

> The burden imposed by the statute to permit deductions for rentals is onerous. Taxpayer must have proved to the trial court that the payments were wrung from it by compulsion of circumstances delineated by law. The question whether surrounding conditions drove the taxpayer through this narrow gate was surely one of fact.

Mere payment, however, of amounts alleged to be for the continued use or possession of property for purposes of the trade or business is not sufficient to establish deductibility in the year of payment. For instance, the deduction under Section 162(a)(3) is limited to amounts which represent rent in fact. In Utter-McKinley Mortuaries v. Commissioner, supra, a substantial portion of the amounts claimed as deductions for rent paid was disallowed as excessive. In many other situations the courts likwise have held that to be deductible as such, amounts claimed as rental or royalty payments must be such in fact within the limits of the statute. E.g., Le Moyne v. Commissioner, 47 F. 2d 539 (C.A. 7th); Limericks, Inc. v. Commissioner 165 F. 2d 483 (C.A. 5th); Hightower v. Commissioner, 187 F. 2d 535 (C.A. 5th); W.H. Armston Co. v. Commissioner, 188 F. 2d 531 (C.A. 5th); White v. Fitzpatrick, 193 F. 2d 398 (C.A. 2d), certiorari denied, 343 U.S. 928; Wade Motor Co. v. Commissioner, 241 F. 2d 712 (C.A. 6th); Beus v. Commissioner, 261 F. 2d 176 (C.A. 9th); Midland Ford Tractor Co. v. Commissioner, 277 F. 2d 111 (C.A. 8th); certiorari denied, 364 U.S. 881 West Virginia Northern Railroad Co. v. Commissioner, 282 F. 2d 63 (C.A. 4th); Potter Electric Signal and Manufacturing Co. v. Commissione 286 F. 2d 200 (C.A. 8th); Fairmont Park Raceway, Inc. v. Commissioner, F. 2d 780 (C.A. 7th); Van Zandt v. Commissioner, 341 F. 2d 440 (C.A. 5t certiorari denied, 382 U.S. 814.

Moreover, the courts have held in general, that rental and royalty payments are not necessarily deductible as such for the year in which paid or accrued, but, rather, for the year or years in which they are properly applicable in order clearly to reflect income. The first such case, Galatoire Bros. v. Lines, 23 F. 2d 676 (C.A. 5th), affirming 11 F. 2d 878 (E.D. La.), involved the taxable year 1917. In that case

the taxpayer leased certain business property for a period of 45 months commencing January 1, 1917, and ending September 30, 1920, "for and in consideration of a monthly rental of two hundred and fifty ($250.00) dollars, payable monthly and fifty (50) per cent of the profits of the restaurant conducted in said building during the years 1917, and the obligation on the part of said lessees to board the lessor and his family during the year 1917." 23 F. 2d 676. The lessor's 50% of the profit for 1917 amounted to $16,971.63, and the cost of meals furnished to the lessor and his family during that year amounted to $2,736. Applicable to the payments at issue in the present case is the conclusion of the Court of Appeals in the Galatoire case (23 F. 2d 676-677) that:

> The lease does not purport to make the promise to pay those amounts when ascertained a part of the consideration for the rented premises during the year 1917 only. By the terms of the lease contract the consideration for those payments was, not the use of the premises during 1917 only, but "the present lease," which was for a term of 45 months. In paying those amounts the lessees paid part of the consideration for the use of the premises for 33 months succeeding the year 1917. The expenditures in question being in part a consideration for the use of the rental premises after the year 1917, the whole thereof cannot properly be considered "necessary expenses actually paid in carrying on any business or trade" during that year, and only the part thereof properly attributable to the process of earning income during that year was deductible from the gross income for that year. [Citations.]"

In many other comparable situations the courts have held that rental payments are deductible only for the year in which they are applicable, or over the term of the lease, rather than in the year of payment. In J. Alland & Bro., Inc. v. Commissioner, 1 B.T.A. 631,

and J. Alland & Bro., Inc. v. United States, 28 F. 2d 792 (Mass.), for instance, the Board of Tax Appeals and the District Court of Massachusetts held that advance rental payment made by a cash basis taxpayer under a lease giving it possession of the leased premises o January 1, 1922, were not deductible from 1921 income.

In King Amusement Co. v. Commissioner, 44 F. 2d 709 (C.A. 6th), certiorari denied, 282 U.S. 900, the taxpayer occupied certain premi under a lease for a term expiring 15 years from May 1, 1911. In 1920, in order to obtain an extension of the lease for an additional 10 years it was required to procure responsible parties to guarantee payment of the rent for the extended period. Two of the taxpayer's stockholders undertook to make such guarantee for a fee of $25,000 each. The $50,000 was paid to them and the extension was executed in 1920, nearly 5 years before expiration of the exising lease. The taxpayer claimed the $50,000 as a business expense deduction on its 1920 return on the ground the payment was neither a bonus nor an advance payment of rent. In denying the deduction, the Court of Appeals said in part (p. 710):

> In the case at bar, the petitioner desired to lease the property at a stipulated annual rental agreed upon with the owner. The owner would not make the lease except upon a guaranty of the payment of the rent, and it became necessary for petitioner to pay Finsterwald and King $50,000 to become guarantors. This was neither an "ordinary and necessary expense" nor compensation "for personal services" in carrying on the business, but was an expenditure for an asset which the petitioner could not utilize for nearly five years. It is true that the payment added nothing to the "value of the lease" or "the rental value of the property." It was none the less an expenditure which it was necessary for petitioner to make to acquire property -- a leasehold to use in its business in the future. In our opinion it was a capital investment, subject to annual allowances for exhaustion during the period of the lease. * * *

To the same effect, see Lichtenberger-Ferguson Co. v. Welch, 54 F. 2d 570 (C.A. 9th); Saks & Co. v. Commissioner, 20 B.T.A. 1151.

The principle of these cases has been uniformly applied in case of bonus and advance rental payments such as involved here. 3/ Particularly applicable here because of similarity of the factual situations are Galatoire Bros. v. Lines, 23 F. 2d 676 (C.A. 5th); Baton Coal Co. v. Commissioner, 51 F. 2d 469 (C.A. 3d), certiorari denied, 284 U.S. 674; Home Trust Co. v. Commissioner, 65 F. 2d 532 (C.A. 8th); Main & McKinney Bldg. Co. v. Commissioner, 113 F. 2d 81 (C.A. 5th), certiorari denied, 311 U.S. 688; Southwestern Hotel Co. v. United States, 115 F. 2d 686 (C.A. 5th), certiorari denied, 312 U.S. 703; Wolan v. Commissioner, 184 F. 2d 101 (C.A. 10th); Cooper Foundation v. O'Malley, 221 F. 2d 279 (C.A. 8th); Bloedel's Jewelry, Inc. v. Commissioner, 2 B.T.A. 611; H. Fendrich, Inc. v. Commissioner, 3 B.T.A. 77; Jos. N. Neel Co. v. Commissioner, 22 T.C. 1083; Fitzsimons v. Commissioner, 37 T.C. 179; Williamson v. Commissioner, 37 T.C. 941.

In Baton Coal Co. v. Commissioner, supra, the taxpayer, on November 14, 1926, negotiated a renewal of a lease under which it was operating certain coal properties. The new lease was to run from November 1, 1926 [date of expiration of the old lease], until

3/ The principle is equally applicable in the converse situation where the lessor spends money or incurs obligations in procuring a lease upon his property, and the expenditure is required to be amortized over the life of the lease. Young v. Commissioner, 59 F. 2d 691 (C.A. 9th); Wells Fargo B. & U. Trust Co. v. Commissioner, 163 F. 2d 521 (C.A. 9th). See also, Bonwit Teller & Co. v. Commissioner, 53 F. 2d 381 (C.A. 2d), certiorari denied, 284 U.S. 690; Central Bank Blcok Ass'n v. Commissioner, 57 F. 2d 5 (C.A. 5th); Griffiths v. Commissioner, 70 F. 2d 946 (C.A. 7th); Commissioner v. Boylston Market Ass'n, 131 F. 2d 966 (C.A. 1st).

all coal had been mined and removed from property covered by the lease. It provided for the payment of $50,000 upon execution and delivery of the lease; for the payment of $51,250 on May 1, 1927; fo payment of a stipulated royalty with a minimum such payment of $26,(annually; for the payment of taxes by the lessee; and for payment to the lessor of one-half of the net profits of the operation. In rejecting the taxpayer's contention that the payments of $50,000 in 1926 and $51,250 in 1927 constituted deductible expenses in the respective years of payment the Court of Appeals said, in part (51 F. 2d, p. 470):

> It is clear that the payments of $50,000 in 1926 and $51,250 in 1927 did not constitute rental payments for these respective years, but together represented the payment of a bonus or rental in advance for the entire term of the lease, the length of which was determinable by the quantity of coal in the ground divided by the average annual output. The lease was to run until exhaustion of the coal. It is clearly evident, therefore, that those sums, together with the other payments specified in the lease, constituted the consideration for a lease during the entire period, and that, under the law and the regulations, those sums must be apportioned as an expense over the whole term of the lease, and are not deductible as a business expense of the year in which they were paid. [Citations.]

In Main & McKinney Bldg. Co. v. Commissioner, supra, the taxpa in 1926, purchased by assignment a 99-year lease on certain real property expiring in 2024, agreeing to assume all of the obligation under the lease and agreeing in addition, to pay as additional rent the sum of $10,000 a year for the first 25 years after the assignme In denying the deduction in full for those years of the $10,000 additional payments made by the taxpayer in 1934 and 1935 the Court of Appeals said in part (113 F. 2d, pp. 81-82):

> For the purposes of this decision, it is immaterial whether these annual payments were part of the purchase price, or were additional rentals; in either event, these sums, together with the other payments specified, constituted the consideration for a lease over the entire period of ninety-eight years. This lease was executed in consideration of cash paid, together with the payments and obligations specified in article two of the contract. Article two named the sums here in dispute. This court is committed to the doctrine that advance payment of rent, made in consideration of a lease for a longer period of time, have the character of capital investments whose benefits are spread throughout the life of the lease, and only an aliquot part of such expenditure is deductible in any tax year. [Citations.]

Southwestern Hotel Co. v. United States, supra, was a suit for refund of income taxes paid for the fiscal year ended August 31, 1935. Southwestern Hotel Co. v. United States, decided March 23, 1940 (27 A.F.T.R. 968). In that case, the taxpayer, on September 1, 1933, leased certain hotel property for a term of 99 years under an agreement which provided for the payment of graduated monthly rentals, and, as "Additional Money Rentals" the taxpayer agreed to make all payments as they became due on a balance of $424,000 on a note secured by a mortgage on the hotel building. This balance was payable over a period of years which period was shorter than the estimated life of the building, to wit, 33 1/3 years. There became due and payable on this mortgage indebtedness during the taxpayer's fiscal year ended August 31, 1935, the sum of $18,000, which amount was paid under the additional money rental provision of the lease. The Commissioner ruled that the $18,000 should be allocated over the life of the hotel building, 33 1/3 years, and allowed a deduction for the year in issue in the amount of $5,280. The taxpayer sued, claiming the full amount of $18,000 as a deduction, and the District Court sustained the Commissioner's determination. 27 A.F.T.R. 968. On appeal, the Court

of Appeals considered the question to be "whether these payments made in satisfaction of the mortgage debt constituted an ordinary and necessary expense paid or incurred during the taxable year in carrying on the business," within the meaning of the applicable statutory provision, and concluded that determination of this ulitmate question is reached "by deciding whether this payment was rental for the use and occupancy of the premises during the particular year in which it was made, or whether it was an advance payment of rental which exceeded the actual value of the use for the year in which it was paid, and which was made in consideration of a lease for a longer period of time." 115 F. 2d, p. 687. It held that the mortgage payment "were clearly advance payments in contemplation of future benefits accruing during the remainder of the lease," and that they should have been spread over the life of the lease instead of over the shorter period representing the estimated useful life of the mortgaged buildin. 115 F. 2d, p. 688.

Particularly applicable here, also, is the statement of the Court of Appeals in Southwestern Hotel Co. v. United States, supra, p. 688, that:

> The fact that these payments were called "additional rentals" in the lease contract can avail appellant nothing. The character of such payments must be determined in the light of the facts and circumstances surrounding them, and the character, not the name, must control. To hold otherwise would defeat the purpose of the act. If the name controlled the fact, this tax could be avoided by the ignorant by chance misnomer, and by the learned by intentional misnomer.

See, also, Cooper Foundation v. O'Malley, supra, and Home Trust Co. v. Commissioner, supra.

Admittedly, the question whether the payments constitute rental expense, on other ordinary and necessary business expense, within the meaning of the deduction statute, rather than advance rentals or capital investments, depends primarily upon the facts of the particular case. In the instant case, the taxpayer concedes that the basic problem is one "of characterizing the payments here in question as current rental expenses or as capital expenditures; and this characterization is dependent upon the underlying purpose for the payments." (Br. 11.) The only evidence in this case of the "underlying purpose" of the payments here in issue is the brief stipulation of the parties (R. 19-22) and the two lease agreements entered into between the taxpayer and the University of Washington (Exs. 3-C and 4-D). The taxpayer's argument (Br. 10-14) that the payments in issue were current rental payments is based solely on the provisions of paragraph 2 of the supplemental lease agreement of February 5, 1958 (Ex. 4-D, p. 3) and the stipulated fact (R. 22) that the payments were recorded in the rental expense account of the taxpayer's books in the years of payment and were recorded by the University of Washington, a tax exempt organization, as rental income for the years in which received.

Paragraph 2 of the supplemental lease of February 5, 1958, relied upon by the taxpayer, provides as follows:

> 2. Lessee will pay to the Lessor the sum of $80,000.00 on November 1, 1960; the sum of $80,000.00 on November 1, 1961; and the sum of $80,000.00 on November 1, 1962, as additional rentals over and above all rentals provided for under the terms of said lease. (Emphasis supplied.)

The "lease" referred to therein is the lease of July 18, 1953 (Ex. 3-C). The provision does not, contrary to the taxpayer's contention, characterize such payments as current rentals, but as "additional rentals over and above all rentals provided for" under the lease of July 18, 1953,

and the Tax Court quite properly pointed out (R. 32) that if the characterization of the payments in the agreement as "rentals" is accepted, it does not necessarily follow that the taxpayer can deduct the full amount in the years paid. There is nothing in the record to demonstrate that they were intended to be, or were in fact, current rentals rather than advanced rentals.

As the Tax Court pointed out (R. 33), the supplemental lease agreement makes no explanation of why the "additional rentals" were to be paid. Moreover, the taxpayer offered no testimony to explain the purpose of the payments. (R. 35, fn. 1.) Also, contrary to the taxpayer's contention (Br. 12), the taxpayer's treatment of the payments on its books and in its tax returns is not determinative of their purpose or character. If this were so, the Commissioner would be precluded from questioning the correctness of a taxpayer's returns. Compare Oesterreich v. Commissioner, supra.

The authorities cited by the taxpayer (Br. 13-14) are not to the contrary. Hyde Park Realty v. Commissioner, 211 F. 2d 462 (C.A. 2d), cited by the taxpayer (Br. 13), so far as the taxpayer's reliance is concerned, involved an alternative contention, unsupported by the fact that advance rentals received by the vendor and credited to the vendee as such upon completion of sale of the property, constituted a reduction of the purchase price rather than rental income to the

4/ So far as the University of Washington is concerned, if it were a tax able organization, it seems clear that such payments would represent income when received. Cf. Commissioner v. Lyon, 97 F. 2d 70 (C.A. 9t); United States v. Boston & Providence R.R. Corp., 37 F. 2d 670 (C.A. 1t) Renwick v. United States, 87 F. 2d 123 (C.A. 7th); Astor Holding Co. Commissioner, 135 F. 2d 47 (C.A. 5th); Hirsch Improvement Co. v. Commissioner, 143 F. 2d 912 (C.A. 2d); Gilken Corp. v. Commissioner, 76 F. 2d 141 (C.A. 6th).

purchaser. One issue involved in Western Contracting Corp. v. Commissioner, 271 F. 2d 694 (C.A. 8th), cited by the taxpayer (Br. 13), was whether the taxpayer was entitled to deduct amounts paid as rentals for certain heavy construction equipment which it first acquired under lease agreements and subsequently purchased at the end of the lease period. In holding that the several lease agreements were not conditional sales agreements, and that the payments in issue constituted rental, the Court of Appeals took into consideration many factors, none of which related to the taxpayer's treatment of the payments on its books. Applicable here, however, is the statement of the Court in Western Contracting Corp. v. Commissioner, supra, p. 699, that "in determining this basic issue, we must look to the intention of the parties and the actual legal effect of the instrument," and cases therein cited.

Benton v. Commissioner, 197 F. 2d 745 (C.A. 5th), cited by the taxpayer (Br. 13-14), is one of the authorities cited in Western Contracting Corp. v. Commissioner, supra, p. 699, and is essentially to the same effect. At issue was the question whether an agreement purporting on its fact to be a lease agreement was, instead, a conditional sales agreement. The Court of Appeals conceived the Tax Court's decision that it was a conditional sales agreement as being based primarily upon objective economic factors rather than upon a determination of the intention of the parties, and on the basis of the Tax Court's own findings the Court of Appeals concluded that the transaction in question was a lease rather than a conditional sale.

The payments here in issue were made pursuant to a supplemental lease agreement, and in the absence of any explanation of their purpose the determination of their character, whether current rental

for possession and use of the demised premises in the year of payment or advance rental paid as part of the consideration for adding the demised premises to the property covered by the original lease, requires a consideration of the terms of the original lease (Ex. 3-C) and the circumstances, as stipulated by the parties (R. 19-22), under which the supplemental lease was executed, as well as the terms of the supplemental lease (Ex. 4-D).

The lease agreement of July 18, 1953 (Ex. 3-C), demised to the taxpayer for a period of 35 years from November 1, 1954, an obviously valuable group of commercial buildings known as the Metropolitan Tract in downtown Seattle. It provided for payment by the taxpayer of annual rental in the respective amounts of $1,600,000, $1,700,000, $1,700,000, and $1,800,000 for the first four years of the lease period, [5/] and a percentage rental for each lease year thereafter equal to specified percentages of the gross rental income received by the taxpayer from subtenants, with a guaranteed minimum rental of $1,000,000 per lease year. The lease further stated that it was understood that all rentals provided therein were predicated on the assumption that the entire demised premises would be capable of being occupied, operated, or used by the taxpayer at all times; and that if for any reason other than default of the taxpayer any portion of th demised premises should not be capable of being occupied, operated, o used by the taxpayer, the annual minimum guaranteed rental should be

5/ As the Tax Court pointed out (R. 35), the fact that the taxpayer paid a fixed annual rental during the first four years of the origina lease has no controlling bearing on the underlying reason for the $80,000 payments here in issue. Moreover, there is no explanation of the reason for fixed annual payments during the first four years of the original lease.

reduced by a proportionate amount for the period of time such space remained untenantable; and the fixed annual rental should be reduced in a like manner of the situation developed in the first four years. (R. 26-27.)

Under the original lease, the taxpayer agreed to modernize the buildings on the demised premises and to expend in such modernization at least $2,000,000, such modernization program to be commenced promptly upon entering into possession of the demised premises and to be completed if reasonably possible on or before November 1, 1958. On the other hand, the lessor agreed to create a "New Building Fund" and to pay a percentage of the gross rental income it received from the demised premises, limited to a certain amount per year, into the fund, which was to be used to reimburse the taxpayer for such modernization expenditures and for the construction of new buildings and major improvements and additions to the property. The taxpayer agreed to study from time to time the desirability and economic necessity for the construction of new buildings and capital alterations, and to make recommendations to the lessor with reference thereto. The lessor had the right to determine what buildings and capital improvements would be made, and the lessee was to be responsible for the construction of such building and improvements with the right to be reimbursed from the New Building Fund for the cost thereof. (R. 27-28.)

On January 29, 1958, the University of Washington reacquired from the United States a part of the post office site which had been carved out of the original Metropolitan Tract in 1902. As consideration for this land, the University agreed to demolish the old post office and to construct a new post office building on that part of the tract retained by the United States. (R. 21.)

The supplemental lease here in issue (Ex. 4-D) was executed February 5, 1958, more than 30 years before the original lease would expire. The most obvious purpose of that agreement was to include th newly acquired post office tract with the properties covered by the original lease. After a number of preliminary recitals, one of which describes the reacquired tract and another of which recites reqcquisi of the tract under a contract which the University agreed to construct a new post office building for the United States, the substanti part of the supplemental lease first provides in paragraph 1 that the described property "shall be deemed to be a part of the demised premi covered by said lease of July 18, 1953, and any new structure located thereon shall be subject in all respects to the rights and obligation of the parties as set forth in said lease with respect to the origina structures upon the demised premises." If further provided that with limiting the generality of the foregoing provision, "it is specifica agreed that monies in the New Building Fund provided for by Article I of said lease dated July 18, 1953, may also be expended with respect the tract of land described in this Supplemental Lease and structure thereon, for the same purposes and in accordance with those same provisions of said lease of July 18, 1953, which govern expenditures out of the New Building Fund with respect to the demised premises, initially described in said lease, and structures thereon."

The supplemental lease next provides in paragraph 2, quoted abc for payment by the taxpayer "as additional rentals over and above all rentals provided for under the terms of said lease" of three payments of $80,000 each on November 1, 1960, November 1, 1961, and November 1, 1962.

Paragraph 3 of the supplemental lease then provided that the taxpayer "shall perform and fulfill each and every of the undertakings and agreements of Lessor under or arising out of Lessor's said contract No. GS-R10-SWPO-A with the General Services Administration of the United States of America, and any and all supplemental agreements relating thereto, at a cost to the Lessor not to exceed the sum of $870,000.00." It was further provided that "For such cost, not exceeding the sum of $870,000.00, Lessee shall be reimbursed out of the New Building Fund established by Lessor under the provision of Article VII of said lease dated July 18, 1953. Any excess of such cost over and above the sum of $870,000.00 shall be borne and paid by Lessee."

The concluding paragraph of the supplemental agreement merely provided that "Except as modified herein, all of the terms, conditions and provisions of said lease shall continue in full force and effect."

To support its contention that the $80,000 payments under the supplemental lease were not made as part of the consideration for including the post office tract and New Washington Building in the leased properties, the taxpayer quotes one of the introductory paragraphs of the supplemental lease agreement as stating the consideration for the taxpayer's right to future use and possession of the tract added to the original leasehold. (Br. 11-12.) This and the other preliminary recitals are indicative of the scope and purpose of the supplemental lease, but the consideration for its execution is stated in the substantive provisions of the agreement noted above. The inclusion of the tract in the leasehold estate imposed upon the taxpayer all of the obligations with respect to that tract, including the obligation to pay rent based upon gross rentals received, which

it had assumed under the original lease with respect to the other properties covered by that agreement. In addition, the taxpayer assumed a further obligation under the supplemental lease to make three payments of $80,000 each on November 1, 1960, November 1, 1961, and November 1, 1962, "as additional rentals over and above all rentals provided for under the terms of said lease," and to carry out the University's contract with the United States "at a cost to the Lessor not to exceed the sum of $870,000.00." Presumably that represented the amount of the University's undertaking, and cost of performing this contract was to be paid out of the New Building Fund, which was the property of the University (Ex. 3-C, Art. VII), to the extent of that amount; and only if the cost of performing that contract should exceed $870,000 would the taxpayer incur any financial obligation on that account. When considered in the light of other provisions of the supplemental lease, and other evidence of record, it would seem naive to suggest that the taxpayer's agreement to perform the University's contract with the Government, at the University's expense, represented the only consideration for adding the post office tract and new Washington Building to the taxpayer's le

Moreover, in the absence of any other explanation, the timing of the $80,000 payments, and the fact that only three such payments were required to be made while the tract added to the taxpayer's leasehold would be subject to the original lease agreement for many more years, support the conclusion that the payments represented consideration fo including the new tract and the new Washington Building in the leaseh There is nothing in the record to associate the payments in issue wit taxpayer's occupancy or use of the added premises during the years of

payment, or to explain their reasonableness as "additional rentals" for the years of payment, or to explain how such "additional rentals" could be justified as rental expense for those particular three years only while the added tract was at all times, including those three years, also subject to the rental provisions of the original lease.

On the other hand, the parties stipulated (Stip. par. 10, between R. 21 and R. 22) that it was decided by the University and the taxpayer that the Douglas Building, smallest and least profitable of the Metropolitan Tract buildings, would be demolished and a new and much larger building constructed on the site. The record does not indicate when this decision was made, or whether it was made incident to reacquiring the post office tract. If the post office tract had not been reacquired, and this decision had been carried out, no additional lump sum rental would have been required under the original lease. It is clear, however, that at the time the post office site was reacquired and at the time the supplemental lease was executed, the parties contemplated a building to occupy both the site of the Douglas Building and the newly reacquired post office tract. The supplemental lease specifically provided that the cost of the new building should be paid out of the New Building Fund. There is no indication in the record as to value of the new Washington Building as an income producing addition to the taxpayer's leasehold estate. It is reasonable to assume, however, that such value was substantial. Likewise, there is nothing in the record to indicate the intention of the parties, at the time the supplemental lease was executed, with respect to when the new building would be constructed. It is reasonable to assume, however, in view of other record evidence, that a timetable for

construction had been agreed upon. Construction of the Washington Building was commenced on July 23, 1958, shortly after the supplement lease was executed on February 5, 1958, and the building was formally opened to occupancy on June 2, 1960, shortly before the first $80,000 payment was due under the supplemental lease on November 1, 1960.

That the three $80,000 payments under the supplemental lease should be timed for the first three years of occupancy of the Washing Building, rather than immediately following execution of the suppleme lease or at some other later period, would not seem to be mere coincidence. Rather, such timing of the "additional rentals" payment seem logically to represent consideration for adding a new and valuab income producing asset to the taxpayer's leasehold estate. 7/ The reacquired post office site and the new Washington Building represent a substantial investment by the University of Washington, which it ha contributed to the taxpayer's leasehold estate, and it would seem justified in demanding some return for the remainder of the lease period over and above the rentals provided in the original lease agreement.

7/ The taxpayer, quoting excerpts from the Tax Court's opinion, argues that "The Tax Court's implied finding that the rent abatement clause was applicable to the transaction in question is clearly erroneous." (Br. 14-15.) The quoted portion of the Tax Court's opin (R. 33-34) cannot be construed as an implied finding. Admittedly, the Tax Court's reasoning is not clear. The so-called rent abatement provision of the original lease (Ex. 3-C, pp. 7-8) may have applied during the period the Douglas Building was untenantable, but there is nothing in that provision to indicate it would apply after the new Washington Building, which replaced the Douglas Building, became tena able, which was prior to the taxable years here in issue. However, even if the Tax Court's reasoning seems confused, its decision nevertheless must be affirmed if it is correct. Helvering v. Gowran, 302 U.S. 238, 245-246; Riley Co. v. Commissioner, 311 U.S. 55, 59; B.F. Goodrich Co. v. United States, 321 U.S. 126, 127; McDonald v. Commissioner, 323 U.S. 57, 64, fn. 7.

In any event, we submit the taxpayer has failed to meet its burden of proving that the "additional rentals" here in issue were in fact payments for the possession or use of the demised premises for the respective years of payment. The Tax Court's conclusion to the contrary is clearly consistent with the facts and the authorities discussed above.

The taxpayer's attempted distinction (Br. 18-22) of the cases cited in the Tax Court's opinion is without substance. As stated above, the question whether an amount is deductible from gross income as "rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity" within the meaning of Section 162(a)(3) is a question of fact to be determined from the evidence in the particular case. The cases cited in the Tax Court's opinion, despite any factual differences, are pertinent authority for the principles for which they were cited, and those principles are applicable to the facts of the present case.

Nor is there any merit to the taxpayer's contention (Br. 22-24) that this Court's review is not limited by the clearly erroneous rule. Not only is the issue involved essentially one of fact, but the taxpayer has produced no convincing evidence to support its claim, and the record presents no basis for reversal.

Not only is this true with respect to the taxpayer's contention (Br. 10-24) that the payments in issue consituted rent within the meaning of Section 162(a)(3), but it also is true with respect to its further contention (Br. 24-31) that in any event the payments represented ordinary and necessary business expenses within the meaning of

Section 162(a) generally.

It is first contended (Br. 24-26) that in denying deduction of payments as ordinary and necessary business expenses the Tax Court applied "an erroneous standard of deductibility" (Br. 24). The contention is based upon a quoted excerpt (Br. 25) from the Tax Court's opinion (R. 36). In commenting upon the inapplicability of certain cases there relied upon by the taxpayer (R. 35), two of which are again relied upon here (Br. 30-31), the Tax Court said (R. 35-36):

> Those case involved the deductibility as business expenses of losses suffered by taxpayers on the sale of stock or securities they had been obligated to purchase in connection with their everyday business operations. Those cases are not controlling here because we are not concerned with losses, and, furthermore, we have no evidence that petitioner was required to make these $80,000 payments in connection with the everyday operation of its business.

The Tax Court's statement is still pertinent with respect to the applicability of the decisions in Commissioner v. Bagley & Sewall Co 221 F. 2d 944 (C.A. 2d), and Booth Newspapers, Inc. v. United States 303 F. 2d 916 (Ct. Cl.), again relied upon by the taxpayer (Br. 30-3

The so-called "standard of deductibility" is spelled out in the statute. To be deductible under Section 162(a), expenditures must be paid or incurred in carrying on the trade or business of the taxp and they must constitute ordinary and necessary expenses of the busi as distinguished from other types of expenditures, such as capital expenditures. See Welch v. Helvering, 290 U.S. 111; Commissioner v. Tellier, 383 U.S. 687, and authorities cited. The deductibility of expenditures as ordinary and necessary business expenses depends upo the facts of the particular case, and a discussion of the authoritie

would serve no useful purpose here because the taxpayer has presented no evidence which would justify characterizing the $80,000 payments under its supplemental lease as ordinary and necessary business expense within the meaning of the statute.

Relying upon the decision in Wyoming National Bank of Casper, Wyoming v. Commissioner, 23 B.T.A. 408 (Br. 27-28), and quoting excerpts (Br. 28) from the introductory recitals in the supplemental lease as indicative of the motivation for including the post office tract in its leasehold, the taxpayer asserts that its obligation to make the payments in issue existed by virtue of contract in order to "fulfill the obligations set forth in the lease agreement of 1953 and the supplemental lease agreement; i.e., to maintain the character of the originally demised premises as a center of store and office buildings of the first class". This, however, is not sufficient to establish the character of the payments as ordinary and necessary business expenses. The facts in Wyoming National Bank of Casper, Wyoming v. Commissioner, supra, were sufficient to establish the business expense character of payments involved in that case, but here, as the Tax Court said (R. 37); "we have no evidence that would bring petitioner's situation within the ambit of that case."

The Tax Court did not err in denying deduction of the payments in issue as ordinary and necessary business expenses.

CONCLUSION

The decision of the Tax Court is correct. It is supported by the facts and the law and should be affirmed.

Respectfully submitted,

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NOVEMBER, 1966.

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Dated: _____ day of November, 1966.

_____
Fred E. Youngman